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Submission

to

The Ontario Committee on Taxation

by

Gas & Petroleum Association of Ontario

January, 1964

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GAS & PETROLEUM ASSOCIATION OF ONTARIO

SUBMISSION TO THE ONTARIO COMMITTEE ON TAXATION

1. Our Association is the Corporate representative and collective voice of many of the utilities, producers, pipeline operators and equipment and appliance manufacturers who make up Ontario's gas and petroleum industry. A list of our Corporate members is set out in Appendix A.

2. In the comments and recommendations on municipal assessment and property taxes under Section I of this Brief, the Association speaks for its members with the exception of the equipment and appliance manufacturers. In the comments and recommendations on The Retail Sales Tax Act under Section II of this Brief and in the comments and recommendations on The Corporations Tax Act under Section III of this Brief, we propose to confine ourselves to taxation matters affecting our public utility members and pipeline operators. We expect that the views of our other members will be adequately expressed in Briefs to be presented by others.

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Section I - Municipal Assessment and Property Taxes

Section II - The Retail Sales Tax Act

Section III - The Corporations Tax Act

SECTION I - MUNICIPAL ASSESSMENT AND TAXATION

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The over-all assessment in Ontario in 1961 for 11 oil and gas companies was $152,600,000 and the total municipal tax paid by all these companies in 1962 was $8,700,000.

Over the past 60 years or more the basis of municipal taxation has remained substantially the same, while the demand on the municipal treasury for education, social services, recreational facilities, roads, sanitation, water supply, etc., has increased

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The over-all assessment in Ontario in 1961 for 11 oil and gas companies was $152,800,000 and the total municipal tax paid by all these companies in 1962 was $6,700,000.

Over the past 60 years or more the basis of municipal taxation has remained substantially the same, while the demand on the municipal treasury for education, social services, recreational facilities, roads, sanitation, water supply, etc., has increased

enormously. The result is that while real property has increased in value, the increase has not kept pace with the demands made on municipal revenue, even with government grants. The pressure on municipal government to produce more revenue has led to numerous inequalities.

This section of the Brief discusses some aspects of this situation.

Real Property Assessment

4. If real property values are to be used as a basis for municipal taxation, the present principles of real property assessment as outlined in the existing Assessment Act are generally acceptable.

However, to be equitable, these existing principles must be properly applied, and it is often in this area that most of the difficulties with our present system arise.

Assessors who use techniques based on Section 35 of the Assessment Act, and who apply these techniques equally to all properties, both residential and business, should be able to arrive at a sound base for distributing municipal taxation.

It is only when assessors meet certain special properties, such as those of strictly regulated utilities and pipeline companies, that Section 35 becomes impractical. Special provision should be made for such valuations and concise instructions should be provided in the Assessment Act, as outlined in Section 41.

Business Assessment

5. The present principles of assessing businesses an additional sum, depending on the type of business, are not as acceptable as the real property principles. The percentages applied now appear to be arbitrary and unreasonable. They bear no relationship to services rendered the business, or to the ability of each business to pay.

If no new source of revenue can be found to replace that now obtained from business tax, and if business tax must be maintained

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then some more logical method of arriving at business assessment should be found.

Special recognition should be given to those industries and businesses which require a heavy outlay in taxable fixed plant, and more particularly to those industries which are subject to strict governmental regulations both as to rates and plant construction.

Special Tax Rate for Industry and Commerce

6. In recent years the Ontario Government, by legislation, provided that the grants paid the municipalities under the Municipal Unconditional Grants Act should be applied to reduce the taxes on properties of residential and farm taxpayers only.

This caused a wide disparity between the mill rates on farm and residential properties and the mill rates on commercial and industrial properties.

In 1962 the disparity was further widened when by regulations under the Residential and Farm School Tax Assistance Grants Act it was provided that in calculating school tax rates, the school mill rate on residential and farm properties would be at 90% of that on other properties.

The result has been a somewhat alarming divergence of the residential and business tax rates. An example of the effects of this policy comes to mind in another Canadian province where in a certain larger municipality at present there is a business tax rate which is more than double the rate applied to residential properties.

When it is considered that businesses in Ontario already pay a business tax in addition to real property tax, we submit that the use of these further devices, in the application of Government grants, adds to an already iniquitous situation.

Uniform Assessment

7. We are firmly convinced that a sound set of uniform workable rules is the only way equity can be obtained. We would suggest that these rules be drawn up by the Department of Municipal

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Affairs after receiving representations from all concerned. There is a nucleus of some 300 trained assessors in the Province who are graduates of the Assessors' course of Queens University and are members of the Institute of Municipal Assessors. This group would be quite capable of carrying out a program leading to equitable assessment throughout the Province and based upon a set of uniform rules as above suggested. While it would be very difficult to re-assess the entire Province at one time, this should not prevent the institution of a proper system of assessment.

Responsibility for Services

8. Real property is carrying a very heavy tax burden and cannot be expected to absorb continuing yearly increases.

Certain municipal services and commodities, such as hydro, and water, are paid for directly by the user. Other services such as garbage collection, sewage disposal, street lighting, fire and police protection are paid for out of the revenue derived from municipal taxation.

As many as possible of the second group referred to above should also be paid for on a direct use basis, thereby eliminating the subsidy to users now being paid by non-users. Sewage disposal, garbage collection, use of expressways and some recreational facilities lend themselves more to a user charge than do other municipal services such as education, police and fire protection, conservation of health, etc., the cost of which must be distributed by some other form of taxation.

Pipelines

9. The arrival of oil and gas from Western Canada has created a rapid expansion of pipeline facilities.

The construction of pipelines in many areas of the Province heretofore untouched, created assessment and tax problems. Many officials at the municipal level have not the slightest idea what value should be placed on them.

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Pipelines

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The construction of pipelines in many areas of the Province heretofore untouched, created assessment and tax problems. Many officials at the municipal level have not the slightest idea what value should be placed on them.

It naturally followed that direction should be forthcoming from the Department of Municipal Affairs. In 1956 a section was placed in the Assessment Act, (now Section 41) setting out rates at which transmission pipelines must be assessed and providing that the Ontario Fuel Board (Ontario Energy Board) designate transmission lines for the purpose of this section. This left distribution lines to be assessed under Section 35 at actual value.

May we draw to the attention of the Committee that there is no material difference between transmission and distribution pipelines. The same materials are used, the same methods of installation and the same methods of operation. It is most logical that both types of line should be subject to the same assessment under Section 41. This procedure would also eliminate the difficult position in which the Ontario Energy Board is placed in having the responsibility to determine which lines are transmission and which are distribution.

Pipelines require a minimum of municipal services. May we therefore, suggest that the rates for transmission and distribution pipelines be the same under Section 41 of the Assessment Act and that the rate schedule be revised to reflect the minimal services required from the municipality. At present the rates for transmission pipelines are based only on cost. Consideration should also be given to the fact that pipelines contribute substantially to the establishment of other taxable industries within the Province.

The level of assessment varies widely from municipality to municipality. For this reason an equalization factor such as presently produced by the Assessment Branch, Department of Municipal Affairs, should be applied to statutory assessment rates for pipelines.

We understand that one member of this Association, whose pipeline facilities in Ontario are dedicated entirely to the transmission of gas, is filing a Brief with the Ontario Committee on Taxation advocating a significant departure from the current method of assessment and taxation of transmission lines. While a method of assessment and taxation of transmission lines on a basis different

from that fixed for other classes of pipelines, such as distribution and gathering lines, would pose some problem of pipeline classification for companies engaged in more than the transmission phase of the business, no doubt any such alternate suggestion will be considered by the Committee.

Assessment of Oil and Gas Wells

10. In accordance with Section 35(8) of the Assessment Act, oil and gas wells are to be assessed with regard to profits. Because of the difficulty in determining profit, a chaotic assessment condition has resulted in wide variances in the assessment of individual wells.

We submit that the Act should be amended to eliminate any reference to profit and that wells be assessed in accordance with normal property value concepts.

Principles of Equitable Taxation

11. In the formation of any taxation system, we recommend the following principles:

1. That the tax be relatively easy to administer.
2. That the tax provide for equality among taxpayers.
3. That there be as broad a tax base as possible so that more people are contributing to the cost of services.
4. That the tax be not detrimental to the economy.

Recommendations

1. Real Property Assessment

   (a) Present principles of assessment should be properly and equitably applied.

   (b) Provision should be made in the Assessment Act for valuation of special properties such as regulated utilities.

2. Business Assessment

   Industries and businesses which require a heavy outlay in taxable fixed plant and industries which are subject to strict governmental regulation should be given special consideration in fixing business assessment.

3. Special Tax Rate for Industry and Commerce

The differential mill rate between residential and commercial-industrial taxpayers should be eliminated.

4. Uniform Assessment

Action should be taken to arrive at uniform assessment throughout the Province.

5. Responsibility for Services

As far as is practical, those who use a municipal service should pay for it.

6. Pipelines

Distribution and transmission pipelines should be assessed at the same statutory rate in the fixing of which rate regard should be had for the minimal municipal services required. In addition, provision should be made for the application of an equalization factor.

7. Wells

Wells should be assessed in accordance with normal property value concepts, without regard to profits.

SECTION II - THE RETAIL SALES TAX ACT

12. The purpose of this section is to bring to the attention of the Committee the following matters which, in our opinion, are unfair or burdensome to our industry, together with our recommendations:

(a) Materials Used in Plant Construction

Regulation 20 Section (1) subsection (d) allows a rebate of tax paid when tangible personal property enters directly into and becomes part of the construction of capital works of a municipal corporation or a local board thereof. It is our interpretation that this would allow a rebate of tax to municipal corporations engaged in the distribution of natural gas. Due to the fact that the same public service is being provided it is our opinion that the charging of tax on capital expenditures of private corporations engaged

in the distribution of natural gas is inequitable since both private corporations and Public Utility Commissions are providing the same service. In addition, the natural gas being delivered is tax exempt.

Recommendation

We would, therefore, recommend that a rebate on tax be allowed to the investor owned corporations engaged in the distribution of natural gas so as to be consistent throughout the gas distribution industry in that natural gas being sold is sales tax exempt.

(b) Repair Parts Charged to Customers

In repairs in which the materials form an insignificant amount of the total charges, tax does not have to be charged on the materials. In the gas industry it is usual for the companies to provide free service on the repair of the customer's appliances and only charge for the material involved and, therefore, under the Act tax must be charged on these repair parts, although they may be an extremely small portion of the total cost to the companies of the repairs. However, in some instances utilities are charging for service, and therefore, the parts are tax free due to the fact that they are an insignificant amount of the total charges. The bookkeeping involved in maintaining records of these repair parts issued to many thousands of customers is burdensome and we feel unjust due to the fact that others performing the same type of work do not have to charge tax. Industry has no objection to the tax, but is looking for an easier way of handling the tax.

Recommendation

We would recommend that tax be paid by the gas companies at the time of purchase as this would eliminate a great deal of record keeping for the minor amount of tax to be collected.

(b)

SECTION III - THE CORPORATIONS TAX ACT

13. The purpose of this submission is to bring to the attention of the Committee the following matters which, in our opinion are unfair to our industry, together with our recommendations:

(a) Some normal business expenses are disallowed in arriving at income for tax purposes. In other cases, uncertainty exists as to their deductibility. In our opinion, all normal business expenses should be deductible in arriving at income for tax purposes and where uncertainty exists, appropriate legislation should be introduced to remove the uncertainty.

(b) Assessment procedures under the Corporations Tax Act allow the Provincial Treasurer too long a period in which to examine a return and issue an original assessment and do not require him to assess loss years.

In our opinion, the Provincial Treasurer should be required to issue an original assessment or a notification that no corporation tax is payable within two years from the date of filing a corporation tax return. Furthermore, a notification that no corporation tax is payable should include an assessment of the business loss, if any, available to be carried forward as a deduction in arriving at the taxable income of future taxation years. A taxpayer who disagrees with an assessment of a business loss should be granted the right of appeal from such assessment.

(c) It is recommended that the capital and place of business tax be completely abolished for the following reasons:

(1) It contributes only a small percentage to the provincial revenue, and the abolishment would facilitate the possibility of a combined return for federal and provincial purposes, thereby making possible lower administration costs for the department which savings would offset somewhat the loss in taxation revenue.

(2) Owing to the factors which determine the payment or non-payment of this tax, it becomes, for practical purposes a tax imposed on business losses, which would appear undesirable and unreasonable.

(3) In so far as it is primarily a tax on companies in their formative stages when profits are negligible or non-existent, it tends to nullify the incentives provided for new establishments by both provincial and federal governments in their respective income tax provisions, and it is definitely contrary to the present admirable efforts of the provincial government to attract new industries and businesses to Ontario.

ECONOMIC FACTORS

14. At this point we would draw the attention of the Committee to certain economic factors which must be taken into account in assessing the merits of our submission:

(a) Gas competes closely with oil and electricity as a source of energy.

(b) By its nature, a gas utility must make a very heavy capital investment in plant and distribution facilities. Important items of cost in operating a gas utility are, therefore, depreciation of these capital assets and the costs of raising the funds required to finance their acquisition.

BUSINESS EXPENSES

15. In general the view of our members is that all expenses chargeable against income in accordance with generally accepted accounting principles should be deductible in computing income for tax purposes. In some cost areas, certain items are allowed as deductible expenses for tax purposes, some are not allowed and for others an element of uncertainty exists as to the tax treatment. Three such areas of doubt are:

(a) Costs relating to capital financing.

(b) Costs of hearings before regulatory authorities.

(c) Costs of rights of way.

Costs Relating to Capital Financing

16. For all public utilities, these costs are of a substantial and recurring nature. The costs can be broken down as follows:

(a) Legal, accounting, printing and incidental costs relative to the preparation of prospectuses and other documents for financing purposes.

(b) Interest and standby charges.

(c) Exchange costs encountered in servicing debt placed in foreign countries. Under this category is exchange arising on -

(i) Payment of interest obligations on debt placed in foreign countries; and

(ii) Repayment of principal on foreign debt.

(d) Commission paid to underwriters for the sale and distribution of securities.

(e) Discounts on securities issued.

Items (a), (b) and (c) (i) are allowed as deductions in computing income for tax purposes. Items (c) (ii), (d) and (e) are not allowed.

17. These costs are proper charges against income under good accounting practice either in the year incurred or on a deferred basis and in our view all should be allowed for tax purposes. The items which are presently disallowed, i.e. commissions paid to underwriters, exchange losses on repayments of debt placed in foreign countries and discounts on securities issued are just as must costs of capital financing as the items which are presently allowed in computing income for tax purposes. We urge the Committee to recommend in its report that these expenses be allowed.

Costs of Hearings Before Regulatory Authorities

18. These are expenditures arising from hearings before

governmental authorities. These hearings are of a recurring nature and include the following:

(a) Hearings covering application for approval to export gas, either from a province or from the country.

(b) Hearings covering applications for approval to import gas from a foreign country at which the company supports the application.

(c) Hearings on applications for certificates of public convenience and necessity which include franchise approval and facility expansion.

(d) Hearings on rate matters, initiated by either the utility or others.

(e) Hearings affecting the utility at which it may act as a third party either as an intervener or supporter of the applicant.

19. The principal items of cost involved in these hearings are professional fees to outside advisers, together with printing and travelling expenses. The deductibility of costs arising from these hearings is not clearly indicated in the Corporations Tax Act and as a result the Provincial Treasurer has not been consistent in his treatment, particularly in cases where the taxpayers' application has been unsuccessful. We submit that these are routine expenses in our industry and that any doubt as to their deductibility should be removed by appropriate amendment to the Corporations Tax Act.

Costs of Rights of Way (including easements)

20. At present, the Corporations Tax Act does not recognize as costs subject to capital cost allowance disbursements relating to the acquisition of rights of way - costs which are very significant in a gas utility. These costs are incurred for the right to install gas pipelines across land owned by others. The costs of rights of way differ from costs of land because there is no salvage value when the rights of way are no longer required. The economic life of the rights

of way ends when the plant facilities located thereon are abandoned or removed. In our view, capital cost allowance on the costs of acquiring rights of way should be permitted in the same manner as on the cost of the facilities.

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All of which is respectfully submitted

this 17th day of January, 1964

F. R. PALIN,
President,
Gas & Petroleum Association of Ontario.

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APPENDIX 'A'

GAS & PETROLEUM ASSOCIATION OF ONTARIO

GAS UTILITY MEMBERS

Central Pipe Lines Co. Ltd.
Consumers' Gas Company,
Great Northern Gas Utilities (Operations) Ltd.,
Public Utilities Commission of the City of Kingston,
Lakeland Natural Gas Limited,
Northern Ontario Natural Gas Co. Ltd.
Provincial Gas Company Limited,
Union Gas Company of Canada Limited,
United Gas Limited,

PRODUCTION MEMBERS

Consolidated West Petroleum Limited,
Haldimand Gas & Oil Limited,
Imperial Oil Limited,
The Petrol Oil & Gas Company Limited,
Roth & Roth Limited,

TRANSMISSION MEMBERS

Trans-Canada Pipe Lines Limited,

MANUFACTURERS

Banister Construction Company Ltd.,
Beach Foundry Limited,
Bristol Company of Canada Limited,
Bryan Donkin Company of Canada Ltd.,
The Canadian Coleman Company Ltd.,
Canada Iron Foundries Limited,
Canadian Meter Company Limited,
Clare Brothers Limited,
Clark Compressor Company Limited,
Contractors Machinery & Equipment Limited,
Corrosion Service Limited,
Crane Supply,
Dearborn Chemical Company Limited,
Denso of Canada Limited,
Dresser Manufacturing Company Ltd.,
Eclipse Fuel Engineering Co. of Canada Limited,
Ellis & Howard Limited,
Emco Limited,
J.R. Fergusson Company Limited,
Findlays Limited,
Gas Machinery Company (Canada) Ltd.,
General Controls Co. (Canadian) Limited,
A.F. Hall Company Limited,
Heath Survey Consultants Limited,
Honeywell Controls Limited,
Jones-Mackey Industrial Limited,
Koppers Products Limited,
Lantz Rhodes Limited,
Lytle Engineering Specialties Ltd.,
Marchand Furnace Limited,
McDace Limited,
Moffats Limited,
Mueller Limited,
The Oil Well Supply Company Limited,
W.H. Olsen Manufacturing Company Ltd.,
Page Hersey Tubes Limited,
Parkinson Cowan (Canada) Limited,
Peacock Brothers Limited,
Rheem Canada Limited,
Roberts-Gordon Appliance Corp. Ltd.,
Rockwell Manufacturing Company of Canada Limited,
Roots-Connersville Blower (Canada) Limited,
G.I. Russell & Company Limited,
Ruud Manufacturing Company,
Shaw Pipe Protection Limited,
Smith International S.A., A.O.,
Robert B. Sommerville Company Ltd.,
Steel Company of Canada Limited,
Tapecoat Company of Canada Limited,
Tappan-Gurney Limited,
Tillsonburg Pipe & Supply Company Limited,
Turret Supply Company Limited,
B.D. Wait Company Limited,
T.C. Walker & Associates Limited,

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